

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the Matter of)
)
Revision to Amend Part 32,)
Uniform System of Accounts for)
Class A and Class B Telephone)
Companies to Raise the Expense)
Limit for Certain Items of Equipment)
from \$500 to \$750)

CC Docket No. 95-60
RM-8448

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AMERITECH'S COMMENTS

The Ameritech Operating Companies¹ ("Ameritech" or the "Company"), respectfully offer the following comments on the Notice of Proposed Rulemaking ("NPRM") released in this docket on May 31, 1995. In that NPRM, the Commission asks for comments on its proposal to amend Section 32.2000(a)(4) of the Commission's rules by increasing to \$750 from \$500 the current limit for expensing, rather than capitalizing, certain items of

¹ The Ameritech Operating Companies are: Illinois Bell Telephone Company, Indiana Bell Telephone, Incorporated, Michigan Bell Telephone Company, The Ohio Bell Telephone Company and Wisconsin Bell, Inc.

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equipment.² The Commission also asks whether a carrier should be permitted to amortize the undepreciated, embedded assets covered by such an amendment and, if so, over what period of time.³

I.

INTRODUCTION

The Commission released the NPRM on the basis of a Petition for Rulemaking filed by the United States Telephone Association ("USTA"). USTA's proposal was to increase the expense limit to \$2000, not the \$750 which the Commission now proposes. USTA also suggested that the carriers be permitted to amortize the previously-capitalized, undepreciated investment in embedded equipment over the remaining life of the account in which the investment is recorded.⁴ Ameritech supported the ideas contained in USTA's Petition for Rulemaking when it was filed over a year and one-half ago,⁵ and continues to support them now, particularly the \$2000

² NPRM at par. 3. The equipment that would be affected by this change include motor vehicles (Account 2112); aircraft (Account 2113); special purpose vehicles (Account 2114); garage work equipment (Account 2115); other work equipment (Account 2116); furniture (Account 2122); office equipment (Account 2123) and general purpose computers (Account 2124). Portable tools and test sets in Account 22XX also are subject to the expense limit. See Responsible Accounting Officers Letter 6, rel. February 27, 1989 at par. 2.

³ NPRM at par. 3.

⁴ United States Telephone 's Petition for Rulemaking, filed March 1, 1994, RM 8448.

⁵ Comments by Ameritech, RM 8448, filed April 23, 1994.

expense limit, as the better alternative to the \$750 limit which the Commission proposes in the NPRM.

However, the most reasonable alternative for companies like Ameritech that operate under pure (no sharing) price cap regulation, is for the Commission to allow such companies to set their own expense limit consistent with industry practice, generally accepted accounting principles and applicable tax laws. This is the alternative which the Commission should adopt in this docket, and the new rule should be made effective January 1, 1995.⁶ If the Commission does not adopt such a rule, it should at a bare minimum adopt a realistic expense limit of \$2000 and allow companies the flexibility to manage their business within that limit. In either event, the amortization of the embedded investment should be the lower of the prescribed depreciable lives or five years.

II.

ARGUMENT

In 1994 before pure price cap regulation was initiated, Ameritech supported the \$2000 expense limit in the USTA proposal for the various

⁶ A January 1, 1995 effective date would be coincident with Ameritech's election of the 5.3 X - Factor effective January 1, 1995. See In the Matter of Annual 1995 Access Tariff Filings Ameritech Petition Regarding Election of 5.3 X-Factor for Application Back to January 1, 1995, Memorandum Opinion and Order, DA 95-1611, rel. July 18, 1995.

reasons summarized in the NPRM.⁷ The telecommunications environment had become considerably more competitive since 1988 when the current \$500 expense limit was established. There had been rapid technological changes since that time, as well. The expense limit proposed by USTA was more reflective of generally accepted accounting principles, would bring carriers' accounting practices more in line with those of comparable, unregulated companies and would allow carriers to react more quickly to technological changes in the future. Increasing the expense limit to \$2000 also would lead to a decrease in administrative and recordkeeping costs. For carriers operating under price regulation, an increase to the \$2000 expense limit proposed by USTA would have little, if any, effect on the carrier's prices for regulated services. For all of those reasons, Ameritech continues to believe that USTA's \$2000 proposal is much more in the public interest than the Commission's \$750 proposal.

The Commission seems to accept the reasonableness of many of these arguments. Specifically, the Commission says:

Because of inflation, the increased competitive environment, and the rapid technological changes that have occurred since the Commission last changed the expense limit in 1988, we [the Commission] believe that we [the Commission] should reexamine the accounting rules related to the expense limit.⁸

⁷ NPRM at pars. 5-6.

⁸ Id. at par. 9.

However, while “generally agreeing in principle that the expense limit should rise,” the Commission tentatively concludes that an increase to the \$2000 limit USTA proposes is “excessive.”

Although it does not say so explicitly, there is more than a hint in the NPRM that the Commission believes USTA’s \$2000 limit proposal is “excessive” due, in part, to the Commission’s concern about whether USTA’s proposal, in fact, would be revenue neutral.¹⁰ The Commission raises this concern because, according to the Commission, USTA’s proposed amortization period would not necessarily equate to the prescribed depreciable lives of embedded equipment and because immediately expensing, rather than capitalizing, new equipment would increase expense at least in the short run.¹¹

However, none of this is relevant for a company, like Ameritech, that operates under pure (no sharing) price cap regulation because increases in its “revenue requirement,” if any, would not be passed on to customers in the form of higher prices. In other words, from the perspective of customers of

⁹ Id.

¹⁰ Id. at par. 10.

¹¹ Id.

pure price cap carriers, any increase in the expense limit necessarily would be revenue neutral.

Therefore, as a company operating under pure price cap regulation, the real question in this docket for Ameritech is whether there is any legitimate reason why the Commission should not abolish the regulatory expense limit and simply allow price cap companies the flexibility to set their own expense limit consistent with industry practice, generally accepted accounting principles and applicable tax laws. After all, if customers are unaffected by the limit, then why shouldn't companies be allowed the flexibility to establish their own expense limits, ones that would bring the company's accounting practices more in line with those of comparable, unregulated companies, that would reduce administrative expenses now and would allow the company to react more quickly to technological changes in the future?

If the Commission does not grant price cap companies this flexibility, then at a minimum it should adopt the \$2000 expense limit which USTA has proposed. The benefit of an expense limit increase to the modest \$750 level proposed in the NPRM generally would be off-set by implementation costs and, therefore, hardly would be worth the effort.

Besides, the \$750 proposal is based largely on the Commission's analysis of inflation. On the basis of that analysis, the Commission concludes

that “an item costing \$500 in 1987 would cost \$635 to replace with 1994 dollars”. Raising the expense limit to \$750 in total, according to the Commission would account for three impacts : first, it “would compensate for inflation over the last seven years”; second, it “would eliminate the need to adjust the cap because of inflation for approximately five years”; and third, it would “recognize the increasingly competitive environment and the rapid changes in technology.”¹²

It is not entirely clear how this analysis supports the Commission’s tentative conclusion. If a piece of equipment costing \$500 in 1987 would cost \$635 to replace seven years later in 1994,¹³ that would translate into a \$20 per year adjustment to the expense limit based on historical inflation alone.¹⁴ If it is reasonable now to establish an expense limit that will not have to be adjusted for inflation occurring during the next five years (i.e., 2000), then a total of twelve years (i.e., 1988 - 2000) of inflation must be accounted for when establishing the new expense limit. If one conservatively assumes that the historical rate of inflation during the period 1987-1994 is an accurate measure of inflation during the period 1995-2000 and, therefore, uses the same \$20 per year amount for the period 1988 (when the expense limit last was changed) to 2000 (five years from now) then, in order to account for inflation alone, the

¹² Id. at par. 9.

¹³ Id.

¹⁴ $\$635 - \$500 = \$135$ divided by 7 years (i.e., 1987 - 1994) = \$20.

amount that should be added to the current \$500 expense limit is \$240 (i.e., 12 times \$20). That results in \$740 and leaves only \$10 (\$750 - \$740) to account for "the increasingly competitive environment and the rapid changes in technology." This \$10 represents 4% of the \$250 increase in the expense limit which the Commission has proposed. It would be patently unreasonable to conclude that this 4% is sufficient to account for "the increasingly competitive environment and the rapid changes in technology" which have occurred since 1988 and which the Commission has acknowledged must be reflected in a new expense limit.

But the real question presented by the NPRM is not how much the expense limit should be increased on the basis of inflation as opposed to the other significant impacts on the current \$500 limit which the Commission has acknowledged. The real question is this: is there any reasonable basis for the Commission to continue to prescribe any expense limit for companies operating under pure price cap regulation? Ameritech believes the answer to that question is "no."

III.

CONCLUSION

Accordingly, Ameritech urges the Commission to allow companies regulated under pure price cap regulation to set their own expense limit for equipment covered by Section 32.2000(a)(4) consistent with industry practice, generally accepted accounting principles and applicable tax laws. This new rule should be made effective January 1, 1995. If the Commission does not adopt such a rule, it should at a bare minimum adopt a realistic expense limit of \$2000 and allow companies the flexibility to manage their business within that limit. In either event, companies should be allowed to amortize the previously capitalized, undepreciated investment in such equipment over the depreciable lives of the equipment, or five years, whichever is less.

Respectfully submitted,

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